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COMMERCE FOR ZHEN GONG-CROSS

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SUBJECT: MONGOLIAN MINING DEBATE SUGGESTS PRESIDENTIAL  
POWER ON THE WANE

Classified By: CLASSIFIED PER DSCG 05-01, REASONS 1.4 B, D, AND E

¶1. (C) SUMMARY. Late into the night on March 2, the Mongolian National Security Council reportedly voted 2 to 1 to approve the long-delayed investment agreement for the Oyu Tolgoi copper-gold project in Mongolia's South Gobi desert region. According to several sources, Prime Minister S. Bayar and Speaker of Parliament Demberel overrode the objections of President N. Enkhbayar. The vote was immediately followed by approval by the Cabinet, which sent the agreement to Parliament on March 4. Parliament, which has been prepped on the agreement, will hopefully approve its terms after what all observers expect to be a spirited debate. This Council vote may mark the beginning of the end of a nearly six-year political journey to gain passage of an investment agreement for the Oyu Tolgoi project. Recounting the history of that journey provides an excellent primer into the evolving relations among the various branches of Mongolia's government. The challenge for Mongolia's political system has been coming to terms with the implications of the new democracy and the constitutional basis for Parliament's dominance over Mongolia's political realms represented in this battle. In addition, President Enkhbayar's inability to enforce his will on the NSC as he did no less than a year ago during a similar debate on Oyu Tolgoi highlights the growing domestic political weakness of his office. END SUMMARY.

2004: The Waning of Socialist Barons  
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¶2. (C) An Oyu Tolgoi (OT) agreement has been a long time coming. Initial attempts to stabilize formally the legal and regulatory framework for this USD 7 billion project began in 2004, but ran afoul of Mongolian election year politics. At that time, Canadian exploration company Ivanhoe Mines held the mining license rights and had been lobbying the senior Mongolian leadership of the ruling Mongolian People's Revolutionary Party (MPRP), led by then-PM and current President Enkhbayar. Ivanhoe's chief legal counsel, John Fognani, explained that the leadership had been extremely encouraging, going so far as to "promise" that they would conclude the deal on its own initiative. Top MPRP leaders asserted that the PM had the power to force an agreement on Mongolia -- regardless of any legal or regulatory requirement to consult with Parliament or the public. Fognani explained that the business community believed a narrow band of post-socialist barons led by Enkhbayar could do what they wanted; and so, businesses had only to deal with them. However, Mongolia had become a functioning democracy by the mid-1990s, and the impact of the vote and a constitution that vested power in Parliament had begun to limit what the socialist era barons could force down the throats of the public or Parliament.

13. (C) A few months before the June 2004 parliamentary elections, the MPRP seniors asked Ivanhoe to delay pushing for an Oyu Tolgoi agreement, asserting that they did not want the Democratic Party (DP) opposition to tar the MPRP as stooges of foreign interests. This admission shocked Ivanhoe and surprised others, because it indicated that Mongolia's democratic system had limited the ability of the political elites to do what they wanted without recourse to Parliament and public opinion.

14. (C) The MPRP barons' political instincts were spot on in 2004. Sensing that the public was quite irritated with perceived MPRP high-handedness, leaders such as Enkhbayar realized that they lacked the power to impose deals on Mongolia and attempted to backtrack from projects in which they appeared to be disposing of Mongolian resources without consulting the public or Parliament. But such backtracking came too late: the MPRP suffered a huge defeat, going from absolute domination of Parliament with 72 of 76 seats to the slimmest of pluralities with 37 seats. The DP won 35 seats and independents claimed four. The DP, along with the independents, used this apparent mandate to block the MPRP at every turn. Consequently, an unsettled political situation ensued until 2008, all but halting progress on major legislation and projects, including on mining projects. A divided Parliament produced divided government. A series of weak coalitions assumed the reins of power; but lacking a solid parliamentary base, none of these governments was willing to risk the wrath of MPs or the public.

2004-2008: Mining plus democracy equals political chaos  
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15. (C) One of the 2004-2008 Parliament's few accomplishments was the 2006 amendment of Mongolia's Minerals Law. The amendment shifted decision making for large-scale mining projects from the government to Parliament. The GOM could negotiate deals but only Parliament could approve agreements on mining development of major social and financial scope. In 2007, the MPRP coalition government led by the former PM, M. Enkhbold, (a former Ulaanbaatar city mayor and currently the lower-ranking of two Deputy Prime Ministers) attempted to use the provisions of the 2006 Minerals law to reach agreement with Ivanhoe and Rio Tinto, which had joined the OT project in fall 2006. Several months of negotiation produced a deal in spring 2007. The deal seemed to have nearly unanimous support among MPs, the business community, and the public, but this support vanished by May.

16. (C) Privately, Enkhbold admitted to post and others that he wanted to move on the 2007 agreement (which most professional observers thought an acceptable, if not a perfect, deal) but feared attacks from the DP, dissident elements within the MPRP, civil society, and, surprisingly, from the President of Mongolia, N. Enkhbayar, whose criticism was particularly troubling.

17. (C) Most observers and stakeholders had expected Parliament to approve the agreement in fall 2007. As far as anyone knew, President Enkhbayar supported the deal, and everyone assumed that the President and PM would unite to pass it in Parliament. It surprised observers when the President and his agents started quietly disparaging the deal, letting it be known that the president could not support the deal unless Mongolia received 51 percent equity at OT. (Note: The 2006 amended minerals law allowed for the GOM to buy up to 34 percent on privately explored deposits and up to 50 percent on publicly-funded minerals exploration. Enkhbayar's proteges in the GOM led the negotiations in spring of 2007, and they crafted a deal that would yield 34 percent of the mine to Mongolia as well as 55 percent of net revenues from the mine, including royalties and other fees. End Note.)

18. (C) Leading negotiators, among them Enkhbayar's formerly-ardent supporter Khurelbaatar (who was then State Secretary of Finance, before becoming the Minister of Finance

then Minister of Fuel and Energy and now an MP) found themselves abandoned by their president, who disavowed any connection to the deal. They claimed to post and others that the president was fully aware of the terms and had supported these arrangements throughout the process, and that they were appalled by Enkhbayar's unexpected and shocking accusations that the government and its negotiators had sold Mongolia out by not getting 51 percent. Summer 2007 saw an explosion of violent comment against the agreement from the DP and the increasingly vocal president. These barrages culminated in September 2007 with media attacks by the president, who explicitly demanded 51 percent or else he would veto the deal.

¶9. (C) PM Enkhbold, in an uneasy relationship with the President and his political supporters in Parliament, was in no mood for a political adventure to save a mining deal that could be used against his government and his party in the run up to the spring 2008 elections. The DP had no intention of supporting a deal that would give the MPRP a development success, and without bipartisan support the agreement was vulnerable to a presidential veto. Consequently, Enkhbold abandoned the 2007 proposal, sending it to Parliament without Cabinet review or preparation. There it languished from fall 2007 to winter 2008, when the new Bayar-led GOM let it die un-voted upon.

¶10. (C) Comment: Reviewing the history of the OT deal from 2003-2008, many observers concluded that it showed that the Mongolian political system vested too much control in the hands of a narrow range of political elites, especially the office of the president. However, these observers were mistaking Enkhbayar's formidable political skills as proof of his office's inherent powers. This might have been true about the office in 2000, but by 2004 the Mongolian presidency had been stripped of many powers observers assumed it had. While PM and an MP, Enkhbayar led Parliamentary efforts to remove the president's power to propose legislation and interfere in the day-to-day activities of Parliament, including the power to approve which party was to form the government. Further, the office required its incumbent to resign from his respective party and all leadership roles therein, effectively removing a base of support within the party from the incumbent. Parliament left the office with a key voting seat on the National Security Council, veto power over legislation (with a two-thirds override possible), and a bully pulpit to issue policy pronouncements but little else. A divided Parliament and weak leadership within the MPRP allowed President Enkhbayar to gain more influence (as opposed to real power) than his position granted to him. It would take the resolution of the DP-MPRP split in Parliament and the coming onto the scene of a skilled MPRP party leader to reveal just how weak the office of president had become. End Comment.

2009: Out of chaos comes political maturity  
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¶11. (C) When Bayar became PM in fall 2007, he told post that he wanted an OT deal. He claimed he could only achieve this through an election in which the public signaled which party it wanted to lead the state. The June 2008 elections gave the MPRP a clear if not overwhelming majority that allowed Bayar to craft a coalition government (or "unity government," to use Bayar's term). The global economic crisis had descended on Mongolia, and Bayar argued that solutions to tricky issues like the OT agreement would require a coalition of the DP and MPRP to resolve outstanding disputes. In practical terms, this coalition has yielded fluid combinations of MPs who grant individual support on a shifting array of issues, but from whom Bayar seems able to craft voting blocs that neutralize the dissidents within and outside of the MPRP.

¶12. (C) Also key to movement on major issues, and especially the OT agreement, was Enkhbayar's very public retraction of his 51 percent position in late 2008. Enkhbayar stated in the press and TV that Mongolia needed the deal for its economic health and that it would be imprudent to stop

progress on OT to get 51 percent. The government should work within the law, which allowed up to 50 percent on some strategic projects, and could always revisit the issue with the companies later, once a deal was struck. (Comment: The economic problems cited by Enkhbayar as justification for moderating his previous hard-line stance were clearly emerging by early 2008. In fact, the more likely explanation for Enkhbayar's change of position in 2008 is that the new political reality of a stable coalition in Parliament and a skilled MPRP leader, Bayar, allowed the inherent powers of parliament and the PM to displace the weakening domestic political power of the presidency. End Comment.)

¶13. (C) This coalition structure allowed Bayar to conclude an acceptable agreement in 2009. First, the coalition in Parliament agreed to create a working group that would set up the terms of reference that would guide the government of Mongolia in its negotiations with private firms that sought to develop the OT project. The working group established a clear set of guidelines for the GOM, which Parliament approved. The GOM was to obtain 50 percent of the property within a certain span of years; a clear revenue stream; environmental, health, labor, and safety protections; value-added production in Mongolia; and would obtain professional advice on this and other strategic projects. The deal was to be negotiated by February 1, 2009, reviewed by the Cabinet and the NSC, and then sent to Parliament for an up-or-down vote no later than the end of February. The dates have slipped and Parliament will not take up the matter until it reconvenes in early April, but the process set out in the Parliamentary decree appears on course.

¶14. (C) Once Parliament had given its chop to the negotiating guidelines, Bayar then set up a clear process within the GOM for negotiating an IA for Oyu Tolgoi. A working group (WG) led by Bayar protege D. Zorigt, Minister of Minerals and Energy, combined elements of his ministry with the ministries of Finance and Environment to handle the day-to-day negotiations with the private firms. The WG would report daily to the PM, the Speaker of Parliament, and the President about progress. In addition, the WG would solicit ideas from MPs on how the deal should be arranged. This was not to allow the MPs any day-to-day role in the process, but rather to give them an opportunity to get their views on record. Post was told by members of the WG that 26 MPs submitted written submissions, of which 17 were accepted and became part of the final agreement.

¶15. (C) Minister Zorigt's personal advisor S. Otgonbat and Oyu Tolgoi negotiating team staffer R. Bat-Erdene revealed that the GOM consulted with Parliament and the President's office to an unprecedented degree. Nothing happened during the negotiations, not a single sub-provision put to paper, that the PM, the Speaker, and the President -- all members of the NSC -- did not know of and agree to. In addition, the WG and Minister Zorigt spent hours in Parliament discussing the deal one-on-one with numerous MPs, answering questions and hearing concerns. Mr. Bat-Erdene explained that this open lobbying by the GOM was a very special, new "trick" devised by Bayar to get the MPs on board before the IA was formally introduced to Parliament. He stated that the approach seems to have gained the assent of coalition members to the basic concepts enshrined in the agreement, if not their complete approval.

¶16. (C) Once agreed to, the deal had its first Cabinet reading before submission to the National Security Council, all of whose members had been informed and approved of its terms. It seemed a simple matter to present it to the Council, which already having signed off on provisions during the negotiation, was expected to quickly approve. By February 15, a deal was on its way to the Council for the assumed pro forma approval. But the NSC did not pass the agreement; rather, a letter was sent in the name of all three members, a letter with eight demands for changes to the deal. Among these were a demand for 51 percent of the project and a demand for the term of the deal to be twenty rather than thirty years. The deal in place vested Mongolia with 34

percent of the equity in the mine upon Parliamentary approval (a 34 percent that Mongolia would have to pay for over time) and the right within one year of Parliamentary approval to buy an additional 16 percent. Nearly all observers attributed this change of heart to President Enkhbayar, who to the surprise of all had apparently decided to return to his hard-line position. The problem with his abrupt turnaround was that the NSC knew the terms of, and had already agreed in principle to, the deal. Further, Enkhbayar's objections were clearly deal breakers that would bring the project to a halt if the NSC insisted on such significant late-in-the-game changes.

¶17. (C) Our sources at Ivanhoe and among the government negotiators argued that that Mongolia desperately needed this deal to improve a collapsing economy that has little else going for it. Success on OT would attract investment in other areas, but what they viewed as Enkhbayar's election year ploy risked alienating companies both foreign and domestic. Mr. Bat-Erdene, who claims to have been present at most NSC meetings, said that a "livid" PM accused the President of risking Mongolia's well being for short-term political gain.

¶18. (C) On March 2, the issue came to a head at a final NSC meeting. The meeting was closed to all but the NSC Secretariat, the three voting members, and the chairman of Parliament's Standing Committee on Foreign Affairs, DP member ¶Z. Enkhbold. The Speaker and the PM insisted that Enkhbayar reverse his position, to seal a deal good for Mongolia. These arguments were punctuated with angry accusations and threats, but Enkhbayar refused to move, at which point a vote was taken that put the president on the losing side.

¶19. (C) This outcome was probably ordained by the political reforms of the last several years, which shifted power from socialist barons and chief executives and vested it in the courts, the government, and the legislature. These reforms stripped the president of his ability to dispense patronage among his party, to impose his legislative agenda or policy preferences on Parliament, to control program execution, and to overturn a government that does not tow his line. Enkhbayar and future presidents now lack institutional levers in the GOM, the MPRP, and Parliament to prevent their positions from being checkmarked.

¶20. (C) Comment. In the past, party barons did not consult with Parliament on deals and laws. Rather, they dumped bills and projects on the legislature for pro forma approval. Of late, the empowered Parliament has taken such treatment poorly and has pushed back on the government and others, strongly asserting its right to deliberate and decide. (Note: In a recent meeting with the Ambassador, Bayar expressed his desire to codify these realities into law and into the constitution, making the position of president purely ceremonial and selected by Parliament, thus removing the position's last electoral vestiges of power. End note.)

¶21. (C) Bayar certainly understands this transformation, but how deeply his proteges and party both comprehend and accept the changes remain to be seen. Rising stars such as Bat-Erdene, Minister Zorigt, and advisor Otgonbat -- MPRP or DP leaders in waiting -- take pride in bringing this deal to Parliament. They recognize that their transparent, consultative model made this accomplishment possible, and hopefully will aid passage of the agreement. For now, it is already clear that the combination of key mining policies and Mongolia's democratic system have positively changed the outlook for Mongolia's political landscape. End Comment.